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PAPER IV- REVIEW OF LITERATURE

TITLE OF THE PROPOSED THESIS
PROBLEMS AND PROSPECTS OF BANK FINANCE TO SMALL AND MEDIUM ENTERPRISES- A STUDY OF SELECTED BANKS IN DAKSHINA KANNADA AND UDUPI DISTRICTS

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1. INTRODUCTION:

Micro, Small and Medium Enterprises (MSME) sector has emerged as a highly vibrant and dynamic sector of the Indian economy over the last five decades. MSMEs not only play crucial role in providing large employment opportunities at comparatively lower capital cost than large industries but also help in industrialization of rural & backward areas, thereby, reducing regional imbalances, assuring more equitable distribution of national income and wealth. MSMEs are complementary to large industries as ancillary units and this sector contributes enormously to the socio-economic development of the country.

Small and Medium Enterprises (SMEs) play a vital role for the growth of Indian economy by contributing 45% of industrial output, 40% of exports, providing employment to 60 million people, creating 1.3 million jobs every year and producing more than 8000 quality products for the Indian and international markets. SME's Contribution towards GDP in 2011 was 17% which is expected to increase to 22% in 2012. There are approximately 30 million MSME Units in India and 12 million people are expected to join the workforce in the next 3 years. SMEs are the fountain head of several innovations in manufacturing and service sectors and are the major link in the supply chain to corporate and the Public Sector Undertakings. SMEs are now exposed to greater opportunities than ever for expansion and diversification across the sectors. Indian market is growing rapidly and Indian entrepreneurs are making remarkable progress in various Industries like Manufacturing, Precision Engineering Design, Food Processing, Pharmaceutical, Textile & Garments, Retail, IT and ITES, Agro and Service sector.

The financing of small and medium enterprises (SMEs) has attracted much interest in recent years. This attention is driven by at least two factors. First, SMEs account for a very significant share of manufacturing and employment, so their viability is important to overall employment levels in an economy. Furthermore, most large companies usually start as small enterprises and the potential of SMEs to develop and invest becomes crucial to any economy wishing to prosper. Second, SMEs tend to be financially constrained and lack of access to finance is an important obstacle to their growth. In fact, in both developed and developing countries bank financing to SMEs is not perceived to be significant. The role of SMEs in the development process continues to be in the fore front of policy debates both in developing countries as well as in developed countries. The

advantages claimed for SMEs are various, including the encouragement of entrepreneurship; the greater likelihood that SMEs will utilize labour intensive technologies and thus have an immediate impact on employment generation; they can usually be established rapidly and put into operation to produce quick returns; and they may well become a countervailing force against the economic power of larger enterprises. More generally the development of SMEs is seen as accelerating the achievement of wider socio-economic objectives, including poverty alleviation. However, the ability of SMEs to grow depends highly on their potential to invest in restructuring and innovation. All of these investments need capital and therefore access to finance is vital. Against this background, the consistently repeated complaint of SMEs about their problems regarding access to finance is a highly relevant constraint that endangers the economic growth of a country.

Role of Commercial Banks in the Promotion of SMEs:

Access to finance has been identified as a key element for SMEs to succeed in their drive to build productive capacity, to compete, to create jobs and to contribute to poverty alleviation in developing countries. Without finance, SMEs cannot acquire or absorb new technologies nor can they expand to compete in global markets or even strike business linkages with larger firms. Well-functioning and sustainable mechanisms for SME financing require institution building and a market approach. Lending institutions must improve their ability to provide financial services to SMEs through commercial mechanisms that lower costs and minimize their risk exposure. Only in this way will financial institutions find SME lending to be more profitable, and thus be encouraged to construct lending programmes targeted at SMEs. There are also a number of trends in the financial services industry that are forcing banks to have a closer look at the SME markets. Globalization trends are increasing competition especially for servicing large corporate customers and driving down margins and fees. The improving liquidity of securities markets in many countries is increasingly providing large corporations direct access to the capital markets and allowing them to by-pass financial intermediaries. Therefore, banks are under increasing pressure to expand their business towards SME customers and to develop mechanisms to improve the profitability of lending to SMEs.

Consequent upon their nationalization, Commercial banks have adopted various promotional measures to augment the flow of bank credit to small scale units. Stress has been laid to reorient

the lending policies with emphasis on need-based, instead of security-based attitude of the commercial banks. The Reserve Bank of India has issued instructions that no worthwhile proposals of the Small Scale units should be rejected merely on the ground that these are not supported by adequate security. The Commercial banks have been advised by the Reserve Bank of India to pay special attention to the needs of priority sector borrowers, particularly of weaker sections, and accordingly they have come up with various schemes for the benefit of small scale units, technical entrepreneurs, rural industries, craftsmen/artisans etc.

Commercial banks constitute the most important source of institutional finance to small scale industries. The banking system is an effective instrument of economic growth, irrespective of the fact whether it is capitalist economy or it is centrally planned. It plays a crucial role in mobilizing the much needed idle resources for investment. Commercial banks have entered the field to provide credit facilities to the small scale units in a big way. They have adopted a liberalized approach in respect of small scale industries, the cardinal feature of such a liberalized approach being the need based credit. The concept of need based credit is to provide assistance tailored to suit the requirements of the small scale units. The needs of a small scale unit would mean not only the total quantum of finance required but also the various types of facilities required. In view of various handicaps and difficulties that the small scale units have to face, the banks are now making necessary relaxation in the terms and conditions of loans, wherever necessary. The lead in providing liberalized credit facilities to SMEs was taken by the State Bank of India and its subsidiary banks. All nationalized banks and other commercial banks also have started showing keen interest in providing the required credit to small scale industries. The State Bank of India has formulated various schemes of providing financial assistance to the SMEs and similar schemes have been adopted by its main subsidiaries. Other commercial banks have also come up with similar schemes.

II) REVIEW OF LITERATURE:

A Literature Review is an account of what has been published on a topic by accredited scholars and researchers. The Literature Review encompassed within this section shows the main themes of the appropriate and relevant finance literature. This review includes prominent empirical studies on problems of finance faced by SMEs and the role of banks in providing finance. This review is meant to provide a rationale for establishing the relevance and importance of the present study. A review of literature pertaining to the current field of investigation is presented in the following two sections: Indian Studies and Foreign Studies.

Financing of small enterprises comprises institutional and Non-institutional Credit (NIC) - finance from banks/financial institutions, and to a greater extent by NIC sources such as trade credit, Non-banking Finance Companies (NBFCs), indigenous money lenders, finance firms, borrowings from friends and relatives, apart from the promoters' own capital. NIC continues to play a greater role despite the efforts to improve the flow of Institutional Credit (IC) to the SME sector. As per the third All India Census of Small Scale Industries, with the reference year as 2001-02, only 14.3% of registered SSI units have availed Institutional Credit; and among unregistered units, as small as 3.1% of units have availed of this facility. The credit from different sources forms an intricate, interdependent, and mutually supportive chain relationship. Trade credit is a crucial and important part of NIC. Inadequacies in credit flow and business relationship between SSI and IC arise because of poor compatibility in their working architectures.

The availability of bank credit is an important prerequisite for the progress of the SME sector. After the implementation of Basel I norms, banks have been reorienting their balance sheets since the early 1990s to comply with the stipulated standards. These have changed the composition of bank portfolios which in turn affected the sectoral deployment of credit. The Reserve Bank of India has issued final guidelines on Basel II norms in April 2007 for implementation from April 2008. These include elaborate prudential guidelines on capital adequacy and market discipline as part of the capital adequacy framework. Areas covered in the guidelines include capital funds, credit charge for credit risk, risk mitigation, and capital charge for market risk and operational risk. Foreign banks operating in India and Indian banks having operational presence outside India should adopt the Standardized Approach (SA) for credit risk, and Basic Indicator Approach (BIA) for operational risk under the revised framework.

Credit for micro and small manufacturing and service enterprises is a part of the priority sector lending as per the latest definitions adopted at the national level for Mass Credit for medium enterprises does not form a part of priority sector lending. Indian Scheduled Commercial Banks (SCBs) have been able to improve their Capital Adequacy Ratio (CAR) after the implementation of banking reforms. This resulted in a much faster investment in government securities as compared to growth in advances. In addition, in the recent years, banks are venturing into non-bank operations like insurance and security-related transactions, which provide them non-bank sources of income. Intensified competition in the banking sector has added to the drive on the part of banks to obtain these alternate sources of income. Finally, options to invest in risk free government securities on the one hand, and to fix interest rates on most advances including the small ones on the other are factors which may have affected the volume as well as terms of credit to those who are only marginally bankable like the poor, and the MSMEs.

Indian Studies:

The access to finance for SMEs represents a topic of great interest for the academic literature, as witnessed by the large number of studies addressing such a problem. Numerous studies based on various surveys highlight that access to finance is one of the most important obstacles in the way of enterprises' growth and development, especially in the case of small and medium enterprises. Here an attempt has been made to make a review of the existing studies on problems of finance to SMEs.

The International Planning Team (Ford Foundation, 1955) concluded that there was a severe lack of capital as well as credit largely because of low productivity and "over-population" in many branches of small industry.

P N Dhar (1958) in his study "Small Scale Industries in Delhi: A Study of Investment Output and Employment Aspect" found that the only source of external finance consisted of relatives, friends and traders.

National Council of Applied Economic Research (1959) in their survey of handloom industry in Karnataka and Sholapur, observed that on the whole, master weavers and money-lenders constituted the major source of funds both in urban and rural centers.

The Society for Social and Economic Studies in their study on "Capital for Medium and Small Scale Industries" (1959), emphasized that the dearth of capital resulted from a low income level, a small capacity to save and hence a lack of capacity to invest.

D.T. Lakdawala & J C Sandesara (1960) in their study on "Small Industry in a big city: A Survey in Bombay" found that 342 firms had 391 cases of borrowing; in 259 firms or two-thirds of the cases loans had come from traders –in 250 cases against raw materials and in 9 cases in the form of cash. 224 or one-fifth of the surveyed small-scale units in Bombay had some difficulties in supply of raw materials, 146 had problems due to small purchases and dependence upon retailers and trade credit, 56 due to import control and similar restrictions and inferior quality of indigenous materials and 22 due to fluctuating prices. Of the 1960 interviewed entrepreneurs, 634 or 60 percent saw no way of improving their technique of production. The difficulties were: lack of finance, lack of adequate demand, government restrictions, lack of space, lack of power supply and inferior quality of products.

Balakrishnan G (1961) in his study on "Financing Small Industries in India :1950-52" analyzed the financial experience of joint stock companies in the small scale sector and found that these had a low profit-earning capacity due to higher cost of production and higher rate of interest.

Baljit Singh (1961) in his study on "The Economics of Small Scale Industries: A Case Study of Small Scale Industrial Establishments of Moradabad" found that of the indebted establishments 33 percent were indebted to traders and dealers, 27 percent to relations and friends and 21 percent to money lenders.

Mishra J N (1962) in his study on "Small Scale and Cottage Industry in Saugor District" inferred that bureaucratic procedures constituted one of the important impediments to the utilization of institutional resources. He found that industrialists preferred a bania (private money-lender) to a

co-operative bank for meeting their financial needs because of complicated formalities, cumbersome procedures and undue delay.

Ramakrishna K T (1962) in his study on "Finance for Small Scale Industries in India" explains the capital and credit needs of SSI by keeping the number of people employed as the basis and analyses the role played by State Bank of India in financing SSIs. Perhaps the effort of Ramakrishna is one of the first in its attempt to assess the capital requirement of SSIs. This study is entirely devoted itself on the financial problems faced by the SSIs.

National Council of Applied Economic Research (1963) in the study "Small Scale Industries of Mysore" found that the highest contribution by financial institutions in Mysore was 41 percent of the total loan that was taken from commercial banks.

UNESCO Research Centre on Social and Economic Development in Southern Asia (1966) in the study on "Small Industries & Social Change" held at Hyderabad, Rajkot, Delhi and Ludhiana found that entrepreneurs had an attitude of "Skepticism" towards Government Policy. In Hyderabad none of the surveyed units had borrowed from the Government or a bank; in Delhi 9 percent had obtained loans from one of these sources and 45 percent in Rajkot.

Administrative Reforms Commission (1969) in their Report of the Working Group on Small-Scale Industries stated on the basis of a survey conducted by the Central Small Industries Organization that on an average only 20 percent of the credit needs of the small-scale sector were being met by institutional sources

Inderjith Singh & N S Gupta (1971) in their study on "Financing of Small Industry" found that their survey in Jammu Kashmir pointed out the inadequacy of institutional credit accounted for only 5.1 percent of the borrowings.

Ramakrishnan (1975) in his study on "New Entrepreneurship in Small Scale Industry in Delhi" found that entrepreneurs were prepared to pay or had paid a much higher rate of interest to non-banking sources to avoid bank formalities.

Pareek H S (1978) in his study on “Financing of Small Scale Industries in a Developing Economy Illustrates the need for finance for SSIs, problem of finance and the present institutional net-work to provide finance. The study is devoted more towards the operations of commercial banks and their schemes to provide finance to SSIs.

Desai V (1979) in his book “Organization and Management of SSIs” deals with the source of finance for SSIs and the requirement of working capital for SSIs. There is also a cursory glance on the commercial Banks Finance to SSIs. Further, Desai traces the history of commercial banks' finance to this sector from 1956 when SBI introduced the Pilot Project Scheme. He also deals in detail the security oriented approach of banks and the terms and conditions of the banks to provide finance to SSIs.

Soundaraj (1980) in his study on “Financing Small Scale Industries- A Profit” states that the Reserve Bank as a Central Bank, Bankers Bank and the Prime Lending Bank to the Government should take initiatives to promote the SME sector. The author stressed that financing the Small and Medium Scale Enterprises in India is very important because SMEs provide more employment than any other sector. As a result the people migrating from villages to cities in search of better jobs and better facilities could be controlled.

Upadhyaya K K (1980) in his study on “Financing of Industrial Growth in a Developing Region” gives the financial spectrum for the industrial sector as a whole. This study gives information on the sources of finance for both large and medium sectors as well as the SSIs.

Brahmanadam G N, Rai H L, Dakshina Murthy D, (1981) in their study on “Financing Small Scale Sector- the Role of Banks” found that during 1981 Indian Banks were not interested in financing the SMEs because of their low credit worthiness. Later due to changes in the industrial policy of India, the commercial banks came forward and rendered immense help to the growth of SMEs. The study was conducted before the economic reforms took place. The authors felt that more analysis was required about the role of banks during the post economic reforms.

Raghava Reddy G (1981) in his study on "Bank Finance for Village and Small Industries" pointed out that village and small scale industries contributed 49 percent of the net domestic product in the manufacturing sector but received only 24 percent of the bank credit. He advocated that the bank credit available to them should at least be equivalent to their contribution.

Jayaprakash Reddy R, Brahmandam G N (1987) in their study on "Small Scale Sector- Problems and Prospects", deals with the various problems like marketing, raw material, labour, technical and financial problems. The study revealed that finance related issues were not yet considered while more focus was laid to procurement of raw materials, marketing and labour problems in SME segment. The authors felt that the main limitation of their study was that it had not discussed about the credit facilities for the SMEs.

Khankhoje D P & Kaveri V S (1992) in their study on "Development of Rural Industries, SSs and Tiny Units and the Role of Banks – A Survey" surveyed 111 units consisting of 41 SSI units, 38 tiny units and 32 village industries or rural industries from four regions of Maharashtra. Data required for the study were collected through the structured questionnaire designed for the entrepreneurs. Through the questionnaire it was attempted to understand their problems related to different stages of bank finance which include: project formulation, project appraisal and credit sanction, project implementation and performance, sickness and rehabilitation of project. The study concluded that delay in credit sanction is the prevalent problem. To sort out this, the present policies, procedures and practices relating to bank lending need a fresh review. To a greater extent this issue can be resolved internally if the bank spells out its data requirements for availing of finance and carries out the entire loan processing in one sitting. In the present trend of liberalization, competitive environment would call for efficient and quick services to the borrower. In this context, the bank is advised to set up a Guidance Cell to offer counseling services to the entrepreneurs. Along with this the bank should organize borrowers meet regularly for mutual understanding of problems and exchange of viewpoints. Such meetings could pave the way towards effectively resolving not only the banker borrower problems but also take care of some of the operational impediments of the units. Finally, motivation of the concerned staff and equipping them with the requisite knowledge and skill particularly in the context of new services such as

counseling, project finance, factoring, etc. would go a long way in increasing the utility of bank services.

Sebastian J (1995) conducted a study titled "Procuring Finance: A Primer for Small Scale Entrepreneurs". The study is based on the author's interactions with small scale entrepreneurs and bank managers in connection with field work for two research studies. One in the North Eastern States and the other in selected centres in various parts of the country. Structured but open-ended interviews were conducted with small scale entrepreneurs and bank managers. Based on interactions with bank managers and small scale entrepreneurs this study attempted to outline a few guidelines for a systematic approach to seek finance, endeavoring to be of help to entrepreneurial aspirants. These are particularly relevant in the context of liberalization which exposes small scale entrepreneurs to a competitive environment. Lending decisions of banks often involve both objective and subjective aspects. Very often small scale entrepreneurs commit the mistake of concentrating only on the objective factors. One of the major reasons for loan turn-down is lack of meticulous planning aimed at influencing the subjective factors behind lending decisions. His study also identified a few crucial aspects which if given due attention, can go a long way in ensuring finance to small scale entrepreneurs.

Mitra S K (1998) in her study titled "Small Scale Industries –Credit Opportunities and Marketing Assistance" concluded that the major factors affecting the flow of credit to the SSI sector can be broadly categorized into two segments. One set of reasons indicated shortcoming inherent in SSI sector which are stated below:

- A weak financial base which eventually prompts the entrepreneurs to bring in funds by way of loan rather than capital.
- Improper maintenance of books of accounts.
- Inability to provide collateral security.
- Delay in payments by the larger units.
- Lack of appreciation of financial data required by banks/financial institutions etc.

The second sets of reasons are attributed to be operational restraints and perceptions of banks and financial institutions which are as follows:

- The administrative cost of lending to small borrowers is relatively high thereby resulting in a disincentive to lend to SSI units.
- High mortality rate/sickness amongst the SSI units.
- The concessional interest rate does not motivate the financial institutions intrinsically to invest in SSI units, etc.

Kaura M V & Sharma G L (1999) in their study on "Financing Small Industries- Institutions should change their attitudes and procedures" identified that attitude of the financial institutions whether centrally owned or state owned or the government agencies promoted for financing small industries needs to be changed. In the wake of the MSME Act (2006) passed in the interest of the Small Scale Sector by the Government of India, the attitude of the financial institutions towards SME sector is totally changing.

Ramachandra K S (2001) in his study on "Reviving Sick Units" discussed the strategies for reviving of the sick SMEs in various aspects like providing technology, management training, skilled labour, export promotion and giving finance . He felt that the root cause for all the problems faced by SMEs is the financial problem. He opined that the financial institutions should provide sufficient amount of credit at an easy disbursal system to promote the SMEs.

Raju (2002) in his study on "Small Scale Industries in the Liberalized Era Beg for Attention", tried to clarify the SME definition that centers round the small scale industries in the absence of a clearly defined medium industry sector in India by visiting the Seoul and Bologna Charters on the SMEs. He reviewed the policy, laws and the regulatory and institutional framework in detail with a view to highlight the fact that the SSIs in India required globally compatible facilitation in order to be competitive both domestically and internationally. The author felt that easy and adequate institutional financial support is necessary but not sufficient condition for the growth of this dynamic and vibrant sector. He envisaged a clear role for the Small Industry Associations on the basis of well-defined criteria. He suggested for a quick enactment of a comprehensive law for the SME sector.

Anitha H S (2003) in her study on "Financial Role of Specialized Commercial Banks – from Entrepreneurs Perspective" focused only on the financial role of specialized commercial banks. The real performance of nationalized commercial banks was assessed with the help of the primary data collected during the survey. An attempt was made to study the attitude and opinions of the entrepreneurs about the services rendered by the banks, problems faced by them in getting the assistance, adequacy of it and their views on further scope for improvement in the present services by taking into account the following:

- The extent to which entrepreneurs have relied on banks to meet their initial capital requirements.
- Sources of the bank for initial capital.
- Adequacy of the term loan sanctioned by banks and the source relied on to meet the shortfall.
- Source of working capital, adequacy of it and the source relied on to meet the shortfall.
- Evaluation of terms of lending.

The study covered a period of 8 years from1992-93 to 1999-2000 of SSI lending in Karnataka. It concentrated on Government owned –controlled commercial banks which have specialized branches to finance and promote small entrepreneurs in the state. 120 sample entrepreneurs were chosen who borrowed money from these banks and were running their small business or enterprises. The study concluded that insufficient lending by the specialized commercial banks in the State has forced the small entrepreneurs to rely on multiple agencies to meet their term loan requirements. Moreover, the banks lack commitment regarding the working capital side of the SSIs. Banks should come forward to consider the opinions of entrepreneurs to facilitate the development of entrepreneurship among poor and weaker sections of the society.

Jaila Saaw (2005) in his study on "Growth of Small Scale Industries in India" observed the growth of Small and Medium Industries in India. He found out that the expected growth was not there because of a lot of root causes mainly due to sickness of the units and the underdevelopment in the SME sector.

Sahney M (2005) in his study on "Banks Asked to Stem Industrial Sickness" tries to express the need for banks intervention in the promotion of the SMEs. The officials of the banks in India belonged to middle class families and were unaware of the industrial promotion and its need.

Singh R K, Garg S K & Deshmukh S G (2005) in their study on "Development of Flexible Strategies by Indian SMEs in Electronics Sector in Emerging Economy" identified various kinds of pressures and constraints faced by the SMEs under the emerging dynamic market conditions and stressed the need for flexibility in developing strategies by Indian SMEs. They found that there was a lack of adequate government support, poor financial conditions and customer support which stood as major constraints as quality, cost and delivery time were the main pressures for SMEs in the electronics sector. Authors felt that the SMEs should develop their own strategies carefully for utilizing their limited resources and improve flexibility in the value chain to get support from customers and suppliers.

Chopra K C, (2006) in his study on "Financing for the Decentralized Sector-Small and Medium Industries" focused on the financing for the SMEs in the decentralized sector. The study vividly discussed about the possible ways to finance the SMEs in the decentralized sector like agricultural based and artisan based SMEs. The author found that there was a gap between the centralized and decentralized sectors in getting finance from the banks. The banks were very much lenient in providing loan facilities to the centralized sector.

Nambiar P C D (2007) in his study on "Financing for Priority Sector" paved the way for the thinking strategy for financing the small scale and medium scale industries by the bank officers. The Government of India through its industrial policy clearly stated that the commercial banks should give priority treatment to the SMEs. The study also discussed the attitude of the bank officials. Their attitude was not sufficient to promote the SME sector because the sector was totally neglected for the last several decades due to the development of MNCs.

National Knowledge Commission (2008) in their interview from a set of 155 start-ups and SMEs identified that 42% of the entrepreneurs found it difficult to obtain early stage finance from banks in India. They also observed that the availability of bank finance was less favorable for enterprises started after the year 2000; because of the reason that most of them were in the knowledge-intensive sectors where "information asymmetry and perceived higher levels of risks had inhibited bank credit availability.

Rani and Rao (2008) in their study on "Financing Small enterprises: Recent Trends" observed that Small and Medium Enterprise sector was a vibrant and dynamic one, and an engine of growth for the present millennium. Financing of Micro and Small Enterprises (MSEs), which was a part of the SME sector, had been given special attention by banks and financial institutions, and was included in priority sector lending. The authors found that in spite of the special efforts, only 14.3% of registered small enterprises had availed institutional credit, as per the 3rd All India Census of Small Scale Industries of 2001-02. From 2000 to 2004, institutional credit for SMEs had shown disturbing trends, despite the high level of liquidity in the banking system and the initiatives taken by the Union Government and Reserve Bank of India (RBI). They examined the recent trends in credit flow to SMEs, in particular, and medium enterprises, in a limited way, from commercial banks and the Small Industries Development Bank of India (SIDBI), and outlined the recommendations of A S Ganguly Working Group and Internal Group chaired by C S Murthy. Innovative approaches and directions for the future were presented in their study. They suggested that SMEs need special treatment through devising special instruments of credit for strengthening their competitiveness.

Popli G Sand Rao D N (2009) in their study on "Service Quality Provided By Public Sector Banks To SME Customers: An Empirical Study In The Indian Context observed that in banking sector, the quality of customer service played an important role, particularly in the context of growing competition and sustained business growth. They attempted to ascertain the service quality provided by Public Sector Banks to Small & Medium Enterprises which played a key role in India's economy. The major findings of the study were:

- Modernization and Communication affects the services to a large extent and there is a need to train the staff for improvement of service to the SMEs customers
- The service quality of private banks is superior to that of Public sector banks.
- Majority of the respondents revealed that the credit flow to SMEs sector was not sufficient and the Government has to initiate necessary steps for making the required funds available easily on convenient terms

- Majority of the respondents felt that the policies for SME Sector of other countries are far better from the policies of India
- Delay in loan application processing due to unhelpful nature of the staff members was the claimed by the majority of the respondents.
- 86% of the respondents opined that the banks ask for collateral security/guarantee from a third party even where the project is been assessed as viable and primary security is adequate.

International Studies:

Boer (1992) in his study on "The Banking Sector & Small Firm Failure in the UK Hotel and Catering Study" reported that most of the small firms in UK experienced insolvencies and bankruptcies. Through a sector wise analysis he found that the hotel and catering industry had the second highest rate of bankruptcy. The author felt that combination of a competitively insecure banking sector and the funding of a large number of small firms with questionable business skills and plans led to the largest number of small firms in the history of the UK to cease trade.

Haron and Shanmugam (1994) in their study on "Lending to Small Business in Malaysia" found that for many Malaysian small business owners, lack of capital resulted from their difficulty in obtaining bank loans. The small business owners felt that commercial banks were not sympathetic to their needs. The authors collected information on the perceptions of Malaysian commercial bank officers towards lending to small business. The study was designed to determine the problems faced by bankers in dealing with small businesses and to determine the extent to which these problems influenced the banker's decision making processes. The authors confined the study to five banks and involved only 49 bank officers. Problems related to the character factor appeared to be the major difficulty faced by the bank officers when dealing with small business customers.

Akhtar (1997) in his study on "Partnership Financing of Micro Enterprises" found that credit availability facilitated the establishment of microenterprises which in turn generated employment opportunities for the poor and enhanced their productivity. The author felt that lending small amounts of money to the poor enabled them to earn reasonably high returns through microenterprises. Partnership financing schemes provided compatible incentives to the banks and

borrowers. Both the parties pursued the goal of maximizing expected profitability of the enterprises.

Wtteruglghe and Jannsen (1997) in their study on "The Role of the Banker in Financing Medium Sized Firms in Belgium: Lender or Advisor" analyzed the role of banks in financing medium enterprises in Belgium. They found that like small firms medium-sized businesses also had preference for self-financing. As far as external funding was concerned, debt was generally the main source. The low debt ratios indicated that, as compared to the large firms, the medium enterprises took less recourse to banks and, as a result, paid little attention to their financial function. The bankers did not play an important role as an adviser either, except when the firm decided to raise funds through the stock market. The authors suggested that greater specialization on the part of the banks is required in order to avoid conflicts of interest arising out of the mismatch between their service priorities and the needs of their clients.

Kotey, B. (1999) in his study on "Debt Financing and Factors Internal to the Business" found that growth is constrained and failure can be caused by financial constraints, and that there are both supply and demand side factors. On the supply side, he noted that banks are less likely to lend long-term finance to SMEs due to risk (which is in itself caused by SMEs "lack[ing] a track record of performance on the basis of which their credit rating could be assessed") and cost ("administrative costs, potential interest income and the risk of default") and on account of lack of collateral. On the demand side, Kotey argues that many entrepreneurs do not wish to use long-term debt finance. Whilst this may be true for some, it is clear that many entrepreneurs are refused finance by banks.

Lane C and Quack S (1999), in their study on "The Social Dimensions of Risk: Bank Financing of SMEs in Britain and Germany" reviewed an important issue in their comparative study of UK and German SMEs' bank lending and their entrepreneurs' attitudes towards risk. They found that the issue of risk which influences both entrepreneurs and banks in the deal making process: entrepreneur's judge the level of risk with which they are comfortable whilst banks assess how risky the entrepreneur is as a lending proposition. Their study gave importance to the issue of risk

given that certain personal characteristics of SMEs may make them more risk-averse or may lead banks to consider them more risky propositions.

Coco G (2000) in his study "On the use of collateral" points out that collateral helps to reduce informational asymmetries and moral hazard problems that arise between banks and entrepreneurs. Collateral can be repossessed by the creditor in case of default thus enhancing creditor protection.

Cressy R and Toivanen O (2001) in their study on "Is there Adverse Selection in the Credit Market?" found that, "better borrowers get larger loans and lower interest rates; collateral provision and loan size reduce the interest rate paid … the bank is shown to use qualitative as well as quantitative information in the structuring of loan contracts to small businesses." In effect, it may, therefore, be that simply because banks approach the lending process in a risk-averse way (in order to protect the funds of savers), and thus turn down a number of propositions perceived to be 'riskier', that there is an apparent 'discrimination' against for example women and ethnic minorities.

Howorth C A (2001) in his study on "Small Firms Demand for Finance" investigated that entrepreneurs tend to seek finance first from their own resources, and then from friends and families, and then from other sources such as banks. Indeed, the money from family and friends is often essential (and often regarded as quasi-equity by the banks) to unlock support from commercial institutions.

Cheah Chor Sooi (2002) in his study on "Right Advice Crucial for Small Businesses Seeking Bank Funding" reported that may SMEs failed to secure loan, not because their businesses were not viable or they did not have collateral but because they had engaged wrong consultants. According to Credit Guarantee Corporation Malaysia (CGC), many SMEs employ consultants to prepare loan applications incorporating business plans that are submitted to the banks, but they themselves are not always clear about the content. The author found that most of the SMEs gave contradictory explanations to bank officers when they were queried about cash flow or modus operandi of their businesses during loan application interviews which affected the decision of the officers while financing the SMEs.

Fergal Bryne (2003) in his study on "Investment: A Harsher Climate for Fund-Seekers the Days of Investors Handing out Cash to Pre-Revenue Businesses are Over- Prospects of Funding for New and Growing Companies" reported that banks were the largest providers of finance to SMEs in general. But the author felt that bank finance was effectively not available to most early-stage and growing businesses as they were unable to provide necessary security for a loan. Bryne found that though the Small Firms Loan Guarantee Scheme was designed to help the small businesses by providing guarantees to the banks and financial organizations only 40% of the firms in UK made use of this scheme.

Rodriguez, A. G (2003) in his study found that Lack of access to finance has been cited as an important problem for SMEs. While information on the financial performance and capital structure of SMEs is generally not available, existing surveys by Fundes, Fedesarrollo and Anif indicate that supplier credit and bank borrowing (including leasing) are the main sources of external SME financing. Based on a 2003 Fundes survey of 687 SMEs whose results are summarized in Rodriguez (2003), access to finance was ranked the second most important constraint (particularly for smaller, industrial and younger firms) in the creation, development or diversification of their economic activities.

Beck, Demirguc-Kunt, Laeven and Maksimovic (2004) in their study on "The Determinants of financing obstacles" reflects, based on a survey that has included 10,000 firms from 80 countries, the fundamental factors to which depends the enterprises' access to finance. The study highlights the relationship between the access to finance for enterprises and their characteristics, such as age, size and propriety structure. The authors find that young firms of small size as well as national ones face greater obstacles when they seek to obtain financial resources. The study also highlights the relationship between the degree of economic and financial development of a country (expressed through the degree of financial intermediation, the level of capital market development, the efficiency of the legal framework, the GDP per capita) and the access to finance for enterprises. The authors demonstrate that in the developed countries it can be accounted a decrease of the difficulties that the firms face when they try to obtain financial resources. Furthermore, the study

concludes that the institutional development is the most important feature that explains the differences between countries in terms of financing obstacles faced by enterprises.

Ogujiuba, Ohuche and Adenuga (2004) have found that generating an entrepreneurial idea is one thing but accessing the necessary finance to translate such ideas into reality is another. Many novel entrepreneurial ideas have been known to die simply because their originators could not fund them, and banks could not be convinced that they were worth investing in. Finance, whether owned or borrowed, is needed to expand so as to maximize profit and given the nature of SMES, there is a need for financing.

Beck, Demirgüç-Kunt and Maksimovic (2005) in their study on "Financial and Legal Constraints to Firm Growth: Does Firm Size Matter" based on a survey realized on firms from 54 countries that small and medium-sized enterprises are faced with financial and legal constraints and corruption issues in a much greater degree when compared with the large firms, thus the impact of these constraints on the firm growth is inversely proportional to the size of the firm. Moreover, the authors also noted that the financial and legal system development and the process of reducing corruption help to relax the constraints faced by small and medium-sized firms.

According to a study by the European Banker (2005) on "SME Finance: Investing in SME Lending" reported on the perceptions on the merits of SME finance that finance varied greatly among banks in different European countries. European Banker examined the extent and type of SME finance was available from different European Banks and the competition presented by other types of finance. It was found that provision of finance for SMEs was a high-risk activity, which generated high transaction costs and low return on investments. The extent of SME finance available and the level of services offered varied greatly from bank to bank in different European countries. According to European Commission (EC) statistics, German banks had shied away from providing bank finance to SMEs while in Ireland and Austria banks have played a prominent role in providing bank finance to SMEs.

Fraser (2005) in the UK Survey of SME Finance (UKSSMEF) reported that some 2.9million SMEs (80%) had used external finance in the previous three years and that the main sources of finance

for start ups are personal savings (65%), bank loan (10%) and friends/family loan (6%). He also found that approximately 900,000 businesses (24%) used term loans and that obtaining finance was reported as a major problem at start up by some 10 per cent of businesses. And as his survey was only of people already in business, it fails to capture all those people who have given up as a result of being turned down for a loan.

Beck and Demirguc-Kunt (2006) in their study on "Small and Medium-Size Enterprises: Access to Finance as a Growth Constraint" highlighted that access to finance is an important growth constraint for SMEs. They suggested that financial and legal institutions can play an important role in relaxing this constraint. The authors also noted that innovative financing instruments can help facilitate SMEs' access to finance even in the absence of well developed institutions.

Klapper L, Laeven L, and Rajan R (2006) in their study on "Entry Regulation as a Barrier to Entrepreneurship" found that financial access can help firms start up and expand their businesses through *inter alia* development of new products and production processes, and investment in human capital. A variety of financial services (credit, savings, insurance, and payment facilities) are crucial for growth in the SME life cycle; however, the focus of this report is on expanding access to finance. Firms often depend on informal sources of funding in the very early stages of their development. External sources, however, become more important as firms start expanding, and their availability can determine decisively the growth trajectory of SMEs.

Kitindi E G, Magembe B A S, Sethibe A (2007) in their study on "Lending decision making and financial information: the usefulness of corporate annual reports to lender" found that creditors, banks and other lenders use business information provided by firms to analyze their present performance and predict future performance. Business information reduces information asymmetry. If an entrepreneur has spent time in developing a comprehensive and a priory business plan at an early stage of the project, the risk perception should be reduced and the likelihood of obtaining capital should increase.

The World Bank Group (2007) in its study on "Bank Financing to Small and Medium Enterprises -Survey Results from Argentina and Chile" analyzed whether the conventional wisdom of lack of

Financing opportunities for SMEs is supported by the data. The group focused on the supply side of the SME loan market and studied in detail the banks' perceptions about lending to SMEs. The Group interviewed a wide range and a significant proportion of banks in Argentina and Chile where it concentrated on banks as they seem to be the main providers of external finance (from the formal sector) to SMEs in Argentina and Chile, and they can also provide key services that capital markets are unable to offer, such as technological or administrative support. The comparison between the two countries was interesting. The approach used to analyze banks was based on on-site interviews with banks' top management, the use of a tabulated questionnaire, and the collection of unique data on bank lending to SMEs, which were not available to the Central Banks of each country. The interviews and data processing were confidential, so banks felt practically no constraint in sharing their information, with the understanding that the data would be reported in an aggregate way, without disclosing each bank's strategy or positions. The questionnaire was designed to address three broad areas: The first area tackled banks' involvement with SMEs. The second area focused on the determinants of the degree of bank financing to SMEs, such as demand factors, competition, corporate strategy, and macroeconomic, regulatory, and institutional factors. The third area attempted to understand the business model and risk management process that banks use when working with SMEs. To conduct the study it interviewed 14 banks in Argentina: six foreign, six domestic private, and two public, which account for 75% of the banking system's total assets. In Chile it interviewed eight banks: four foreign, three private domestic, and one public, which represent 79% of the banking system's total assets. In each bank, the team tried to carry out separate interviews with the general manager (to understand the determinants of the bank's involvement with SMEs), the SME business manager (to assess the business model for dealing with SMEs), and the credit risk manager (to comprehend how risks are controlled). The main findings of the study were: First, SMEs have become a strategic sector for banks. This reflects a gap in perceptions since it contradicts the common belief that banks are not interested in serving the SME segment. Second, banks are focusing on SMEs because they perceive that the segment's elevated profits will more than compensate for the higher implied costs and risks; they consider that the SME lending market is large, unsaturated, and prospects are optimistic. Third, since banks have developed coping mechanisms, there are no significant obstacles impeding banks from entering the segment. Fourth, risk management is separate from sales, mostly centralized but not largely automated. The business and risk models do not yet reflect

the complexity of SME lending, so knowing the client is still crucial. Fifth, banks are developing the structure to deal with SMEs: they are adapting their business and risk models to reduce the cost and risk of the segment. The group concluded that banks have discovered a key, untapped segment and are making substantial investments to develop the relation with SMEs.

David I & Jonathan M S (2008) in their study on "Barriers to raising bank finance faced by SMEs" identified the barriers to raising bank finance faced by UK small and medium-sized enterprises (SMEs), specifically the impact of personal characteristics (ethnicity, gender and education). They developed a conceptual model which was tested by analyzing the results of a telephone survey of 400 SMEs conducted by the Barclays Bank small business research team on their behalf. The survey was based on a large stratified random sample drawn from the Bank's entire SME population. They found that education made little difference to sources of finance, except that those educated to A-level more frequently used friends and family and remortgaged their homes. However, graduates had the least difficulties in raising finance. Perhaps surprisingly, women found it easier to raise finance than men. The survey confirmed that ethnic minority businesses, particularly black owner-managers, had the greatest problem of raising finance and hence relied upon 'bootstrapping' as a financing strategy.

Olutunla and Obamuyi (2008) in their study on "An empirical analysis of factors associated with the profitability of Small and medium enterprises in Nigeria" pointed out that the Financial system in every country play a key role in the development and growth of the economy, although the ability to play this role effectively and efficiently largely depends on the degree of development of the financial system. The traditional commercial banks which are key players in the financial systems of nearly every economy, have the potential to pull financial resources together to meet the credit needs of SMEs, however, there is still a huge gap between supply capabilities of the banks and the demanding needs of SMEs.

Stephanou C and Rodriguez C (2008) in their study on "Bank Financing to Small- and Medium-Sized Enterprises (SMEs) in Colombia" analyzed both trend and structure of the SME financing market in Colombia. They found that banks in the country regard the SME segment as an attractive business opportunity though their level of sophistication in terms of business models and risk

management tools remain modest. The authors concluded that the market is characterized by a number of institutional and policy constraints, which inhibits further growth of SME lending.

Atieno R (2009) in his study on "Linkages, access to finance and the performance of small-scale enterprises in Kenya" observed that access to external finance was needed for new SMEs to start and expand operations, develop new products, invest in new staff or production facilities. The author felt that availability of finance for investment in positive net present value projects was vital to the sustainability and viability of new SMEs. Atieno found that a vast majority of new SMEs depended on internal finance (contribution from the owners, family and friends). Internal finance was often inadequate for new SMEs to survive and grow. He felt that it was increasingly difficult to keep the costs within the constraints of self-financing. Therefore, the author concluded that new SMEs needed capital from external sources.

Mercieca S and Scheack C (2009) in their study on "Bank Market Structure, Competition and SME Financing Relationships In European Regions" analyzed how the concentration and competition in the European banking sector affected lending relationships between small and medium sized enterprises (SMEs) and their banks. The empirical evidence suggested that concentration and competition captured different characteristics of banking systems. Using a unique dataset on SMEs for selected European regions, the authors investigated the impact of increasing concentration and competition on the number of lending relationships maintained by SMEs. They found that competition had a positive effect on the number of lending relationships.

National Council of Small and Medium Sized Private Enterprises in Romania (CNIPMMR) (2010) in its study highlighted the main difficulties faced by the SMEs in their relation with the banks. Thus, 82% of the interviewed entrepreneurs considered that the access to bank financing is very difficult, especially because of the excessive bureaucracy, the unjustified high requirements, the high interest rates, the rigidity of the creditworthiness indicators used by banks, the numerous types of commissions and fees required. Also, over 61% of the SMEs' entrepreneurs and managers reported banks' lack of transparency (by charging hidden fees, ineffective communication etc.), no real negotiation (by using standard contracts, banks' refusal to modify or complete the credit contract, etc.) and unjustified and abusive contractual terms practiced by banks (such as

performing unauthorized transactions in accounts and in general bank frauds). The knowledge of these difficulties has a vital importance regarding the need to adopt measures in order to support and improve the SMEs' access to finance.

Ardic, Mylenko and Saltane (2011) in their "Small and Medium Enterprises: A Cross-Country Analysis with a New Data Set" analyze, using statistical data, the macroeconomic and institutional factors that are influencing the SMEs' financing through loans. Similar to other studies, the authors have found a positive correlation between the overall economic development (measured by per capita income) and financial development (measured by the ratio of private credit to GDP), on the one hand, and the SMEs' financing level, on the other side. Moreover, the authors demonstrate that the financing level of SMEs depends also on the legal framework and the overall business environment.

Rocha, Roberto, Farazi, Subika, Khouri, Rania and Pearce, Douglas (2011) in their study on "The Status of Bank Lending to SMEs in the Middle East and North Africa Region: The Results of a Joint Survey of the Union of Arab Bank and the World Bank" investigated the status of bank financing to SMEs in the Middle East and North Africa (MENA) based on a survey of 139 banks in 16 countries. The authors found that in spite of a positive perception of the attractiveness of the segment, the SME sector in the region remains largely underserved. Direct government interventions through public banks, credit guarantee schemes and other forms of subsidized financing play a major role in SME lending, partly compensating for the low level of private sector involvement, which in turn reflects the MENA's weak financial infrastructure.

The perusal of literature reveals that small and medium enterprises face a lot of problems, and inadequate financing is the major one. A rich literature house has been developed overtime, mostly in foreign countries with regard to SME financing. A very few studies have been conducted in India regarding the effectiveness of SME financing schemes of the banks. In spite of the importance of the topic, relatively little research exists on whether, why and how banks finance SMEs around the world. This is compounded by the fact that comprehensive data on SME finance is still to be more consistently collected and monitored over time. Nonetheless, existing studies show that, contrary to the conventional perception that financial institutions are not interested in

dealing with SMEs, banks consider the SME segment strategically important. If SMEs cannot find the financing they need, brilliant ideas may fall by the wayside and this represents a loss in potential growth for the economy. That is why a need was felt to conduct a study to ascertain the wide gap in demand and supply of finance to SMEs in Dakshina Kannada & Udupi Districts of Karnataka, in a bid to offer proposals to overcome their growing needs for finance. Studies relating to SMEs, their problems and source of financing have been undertaken but regarding the SME financing schemes of banks has not been extensively researched. This gap has been identified and it has led to the present research to be undertaken. So, the need was felt to cover the areas neglected. It is therefore necessary to undertake an independent enquiry at the District level. In this direction the present study makes an attempt to highlight the problems faced by the SME sector regarding obtaining finance from banks.

III) <u>STATEMENT OF THE PROBLEM:</u>

Report of Prime Minister's Task Force On Micro, Small and Medium Enterprises, Government of India, January 2010 found that **a**lthough Indian MSMEs are a diverse and heterogeneous group, they face some common problems, major ones are: Lack of availability of adequate and timely credit; High cost of credit; Collateral requirements and Limited access to equity capital.

Access to adequate and timely credit at a reasonable cost is the most critical problems faced by the SME sector in India. The major reason for this has been the high risk perception among the banks about this sector and the high transaction costs for loan appraisal. Despite its commendable contribution to the Nation's economy, SME Sector does not get the required support from the concerned Government Departments, Banks, Financial Institutions and Corporates, which is a handicap in becoming more competitive in the National and International Markets. The statistics compiled in the Fourth Census of MSME sector September 2009 revealed that only 5.18% of the units (both registered and unregistered) had availed finance through institutional sources, 2.05% had obtained finance from non-institutional sources and the majority of units i.e. 92.77% had no finance or depended on self finance. Therefore, the need of the hour is to ensure access of banking facilities to the SME sector. Financial inclusion, including MSME finance and the drive to universal access is the national mandate. Financial inclusion makes growth broad based and sustainable by progressively encompassing the hitherto excluded population.

An exclusive study on the problems and prospects of bank financing to SMEs has not been undertaken so far. There is no comprehensive study covering the District of Dakshina Kannada and Udupi about problems of bank financing to SMEs. There are very few studies pertaining to Karnataka but still these studies do not focus on the financial aspects or on the role of bank finance for the development of SME sector.

IV) OBJECTIVES OF THE STUDY:

The present study intends to identify the problems associated with bank finance on the growth of small and medium enterprises in Dakshina Kannada and Udupi Districts of Karnataka. The main objectives of the study are:

- To analyze the growth of small and medium enterprises in Dakshina Kannada and Udupi.
- To examine the role of banks in the promotion and growth of small and medium enterprises with particular reference to loans sanctioned and disbursed by the banks – sector wise, area wise and industry wise.
- To identify the extent to which SMEs have relied on banks to meet their initial capital requirements.
- To find out the extent to which banks have rendered assistance, provided incentives to the small and medium enterprises in Dakshina Kannada and Udupi.
- To understand the problems of SMEs in availing bank credit and to give suggestions for the mitigation of the same.
- To check the satisfaction level of SMEs regarding SME financing schemes of the banks.
- To know the effectiveness of various SME financing schemes of the banks.
- To identify core constraints faced by SMEs to have access to bank finance in Dakshina Kannada and Udupi and other pertinent obstacles in the growth and development of SMEs.

V) RESEARCH DESIGN AND METHODOLOGY:

This survey based study is exploratory in nature. The primary data is collected through a well designed questionnaire consisting of the questions relating to the problems and prospects of bank financing to the SME sector in Dakshina Kannada and Udupi Districts. The qualitative cum

quantitative research techniques will be utilized to discover solutions for Problems of Bank Financing to SMEs in Dakshina Kannada and Udupi Districts.

An extensive study of the selected banks will be undertaken in Dakshina Kannada and Udupi districts which cater to the needs of the SME sector. Since, the study is detailed one; it is not practically possible to cover all the banks functioning in the districts under study. The Bank Managers of the selected Banks will be personally interviewed and discussions will be held with the help of pre-designed questionnaire to collect their opinions relating to various aspects of the bank financing to SMEs. A comprehensive questionnaire will be prepared for the proprietors of the selected SMEs and they will be interviewed personally with a view to identify the problems they have faced in getting finance from the banks.

Further the secondary data would be collected from books, journals, news papers, internet/ online sources, etc. In particular, data will be extracted from the publications of Reserve Bank of India, research papers, websites, and other various authentic data sources. The reports submitted by various Committees/Commissions relevant to the study will be refereed and these data will be incorporated wherever necessary to substantiate the primary data.

VI) TOOLS TO BE USED IN THE STUDY:

To analyze the data collected statistical tools like percentages, ranking, co-relation and statistical tests like chi-square test, t-test, F-test and Z-test, ANOVA tests will be used depending upon the nature of the data. For generating the statistical results statistical packages like SPSS (Statistical Package for Social Sciences) will be made use of.

VII) SIGNIFICANCE OF THE STUDY:

SMEs are vital for economic growth and development in both industrialized and developing countries, since they play a key role in creating new jobs. Financing is necessary to help them set up and expand their operations, develop new products, and invest in new staff or production facilities. Many small businesses start as an idea from one or two people, who invest their own money and probably turn to family and friends for financial help in return for a share in the business. But if they become successful, there comes a time for developing SMEs and they need new investment to expand or innovate further. This is the area where they often run into problems,

because they find it much harder than larger businesses to obtain finance from banks, capital markets or other suppliers of credit. A crucial element in the development of the SME sector is access to finance, particularly to bank financing, given the relative importance of the banking sector in serving this segment. A number of studies have shown that financing is a greater obstacle for SMEs than it is for large firms, particularly in the developing countries, and that lack of easy access to finance adversely affects the growth of the SME sector more than that of large companies (Schiffer and Weder, 2001; Beck et al, 2005; Beck et al, 2006). It is, therefore, unsurprising that the international development community has listed SMEs access to finance as an important policy priority.

In spite of the importance of the topic, relatively little research exists on whether, why and how banks finance SMEs around the world. This is compounded by the fact that comprehensive data on SME finance is still to be more consistently collected and monitored over time. Nonetheless, existing studies show that, contrary to the conventional perception that financial institutions are not interested in dealing with SMEs, banks consider the SME segment strategically important. Yet institutional constraints remain and the market is far from saturated. If SMEs cannot find the financing they need, brilliant ideas may fall by the wayside and this represents a loss in potential growth for the economy. The present study focuses on the significance of bank financing for the development of SME sector in Dakshina Kannada and Udupi Districts.

VIII) RELEVANCE OF THE STUDY TO THE PRESENT DAY PROBLEMS:

Every Bank has given highest importance to financing SMEs in their strategically growth plan. It has become necessary to bring policy shift and create free market environment from regulations & interventions in economic activity. Growth resulting from globalization and liberalization is visible most profoundly in the SME segment. The relationship between the banker and the customer has become most crucial and competitive. The role of bank credit in the growth of the economy and the SME sector is well-known but access to timely and adequate bank finance is still a distant dream for majority of the units in the SME sector. The government is also not happy with the level of credit flow to the SME sector. Hence, in all the forums, the issue related to extending credit to this sector is discussed. Though many measures have been announced by the government from time to time, for giving a fillip to the SME sector, the government expects banks also to initiate measures so as to double the flow of credit to SMEs. Banks usually are reluctant to lend to

SMEs because of the high transaction costs and perceived risks of SME lending, in the face of insufficient credit information, inadequate credit appraisal and risk management skills, poor repayment records, limited market power, high share of intangible costs, absence of adequate accounting track recording, low mortality rates, etc. The biggest operating constraint for the banks is that officers are personally held responsible for default of smaller loans.

Banks have a vital role to play in addressing several problems faced by the sector today. Banks have to view themselves not just as providers of credit but as partners in the growth of these enterprises, through a process of hand holding of first generation entrepreneurs, while they find their feet in the business. Banks should provide financial consultancy / financial management services to their SME borrowers to give them holistic guidance and support and nurturing them. Bank branches need to ensure greater participation in the affairs of their SME clients by convergence of credit services and non credit services. For this, bank staff should be trained through customized training programmes to meet the specific needs of SMEs such as knowledge of markets, both domestic and global, use of technology, etc. Banks need to innovate to create products specifically suited to the requirements of SMEs and should take a longer term view of its relationship with such entities while pricing such products.

The present study is an attempt in analyzing the problems and prospects of bank financing to SMEs in Dakshina Kannada and Udupi Districts of Karnataka State and the role played by banking institutions in promoting industrialization in the Districts. Certain suggestions and recommendations will be made in the study for the policy makers to implement the various schemes for the overall development of SME sector.

IX) CONTRIBUTION TO THE FIELD OF KNOWLEDGE:

The present study is an attempt at analyzing the problems and prospects of bank financing to SMEs in Dakshina Kannada and Udupi Districts of Karnataka State and the role played by banking institutions in promoting industrialization in the District. Though a number of studies have been undertaken regarding SMEs in general and promotional activities undertaken by the Government and by various developmental agencies in particular, much has not been highlighted on bank financing to SMEs. Hence, the present study is an attempt to fill the gap that exists in the literature

on problems and prospects of bank financing to SMEs in India and with special reference to Dakshina Kannada and Udupi Districts of Karnataka State.

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